STATE OF MAINE
PUBLIC UTILITIES COMMISSION

Docket No. 96-053

January 28, 1997

ROBERT D. COCHRANE ET AL. V.
BANGOR HYDRO-ELECTRIC COMPANY
Request for Commission Investigation
Into Bangor Hydro-Electric Company's
Practice of Installing or Monitoring
Security Alarm Systems

ORDER

WELCH, Chairman; NUGENT and HUNT, Commissioners

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I. SUMMARY OF DECISION

In this Order we establish the requirements with which Bangor Hydro-Electric Company (BHE) must comply to operate its CareTaker security alarm non-utility business venture. We permit BHE to conduct these activities subject to conditions described below. In particular, BHE will be required to establish a separate subsidiary for its non-core utility activities; file annual reports; limit use of certain customer information; and account for these activities "below-the-line."

II. PROCEDURAL BACKGROUND

On February 2, 1996, Robert Cochrane and 23 other persons filed a complaint with the Commission pursuant to 35-A M.R.S.A. § 1302. They asked the Commission to open a formal investigation "for the purpose of stopping Bangor Hydro-Electric Company from engaging in the business of installing and monitoring security alarm systems." After hearing from various interested parties, including BHE, and reviewing a recommendation from its staff, the Commission decided on May 17, 1996, to investigate further some of the issues raised by the complaint.

The Commission stated it wanted to consider the proper level of regulatory review for such non-core utility business ventures undertaken within the utility rather than through a separate subsidiary. It noted that if these activities were taking place in a separate subsidiary, the utility would require approval under 35-A M.R.S.A. § 708 upon organization of the subsidiary, as well as approval of certain transactions between the subsidiary and parent corporation under 35-A M.R.S.A. § 707. Therefore,

> [a] similar review may be necessary if the same activities are undertaken within a utility rather than in a separate subsidiary. After we determine the proper level of review, we will apply that review to the facts of this case related to BHE's security alarm activities.

Order, Docket No. 96-053 (May 17, 1996) at 2.

Following a prehearing conference on June 7, 1996, the parties were asked to file legal briefs on what they believed to be the proper scope of this proceeding. The Public Advocate, the consolidated intervenors representing security alarm businesses including Mr. Cochrane, and BHE filed briefs on June 26, 1996.

After considering those briefs, the Commission found that the primary focus of this investigation would be on establishing

the proper procedures to ensure that utility ratepayers are insulated from any financial risks of the non-core business venture. The investigation would seek answers to the following questions:

1. What cost allocation procedures should the Commission adopt to protect BHE's core electric business customers from any risks associated with BHE's security alarm business?

2. What specific categories of costs should be assigned between non-core and core utility activities (e.g., employees, building, equipment, goodwill, etc.)?

3. What recordkeeping requirements are necessary to ensure the costs of both core and non-core activities may be properly reviewed by the Commission?

4. What specific cost methodology should be employed in calculating and recording costs to be assigned or allocated (e.g., fully allocated, incremental)?

5. What reporting requirements, if any, should the Commission adopt for notification to the Commission when a utility enters a non-core business venture? Are any on-going reporting requirements necessary?

6. Are additional protections needed to protect BHE's core business customers that cannot be adequately addressed through proper accounting procedures? If so, what are they and how should they be implemented?

Order, Docket No. 96-053 (July 12, 1996) at 1-2.

Since any decisions about accounting treatment of this non-core business activity will have a precedential effect for the treatment of non-core activities undertaken by other utilities, notice of the proceeding and an opportunity to intervene was extended to all electric and gas utilities.[1] The following parties were permitted to intervene in the investigation: Robert Cochrane, David Haynes, Thomas Drummey, the Public Advocate, National Burglar and Fire Alarm Association, National Federation of Independent Business, Industrial Energy Consumer Group, Central Maine Power Company (CMP), Maine Public Service Company, the Electricians' Examining Board for the State of Maine, Don Thayer and Gene Ellis.

[1]On May 28, 1996, CMP filed a proposed term and condition that would allow it to provide various energy-related products and services that it characterized as "non-electric." The filing raised questions about whether such services needed to be tariffed, what charges were permitted, and whether these services were regulated. Since many of these issues were similar to those being reviewed in the Cochrane investigation, the Commission decided to examine the generic issues in the Cochrane case first and then take up any issues relevant to CMP's term and condition following completion of the Cochrane case. Intervenors in the CMP case who were not already intervenors in the BHE case were made parties to Docket No. 96-053. *Central Maine Power Company, New Term and Condition § 1.11*, Docket No. 96-285, Order (Aug. 22, 1996).

BHE prefiled the testimony of Peter Dawes and Rich Rusnica on July 29, 1996. The following intervenors prefiled direct testimony on September 11: Robert Cochrane, Curtis Call on behalf of CMP, and Scott Rubin on behalf of the OPA. Hearings were held on October 24, 1996.

By Procedural Order issued on October 28, the parties were directed to brief the six issues contained in the Commission's July 12 Order, as well as the following three related areas:

- How should the Commission define regulated/non-regulated services or core/non-core activities?
- Should royalties be imposed for the use of the utility's name, reputation, or for other purposes?
- Should the Commission adopt rules/or implement policies for Maine's electric utilities based on the FCC's accounting rules for telecommunications carriers, parts 32 and 64?

BHE, OPA, CMP and Mr. Cochrane filed Briefs on November 15 and Reply Briefs on November 22, 1996. A Hearing Examiner's Report was issued on December 10, 1996. Only CMP filed exceptions to that Report. The Commission considered the Hearing Examiner's Report and exceptions at its Deliberative Sessions on January 13, 1997 and January 27, 1997.

III. DESCRIPTION OF BHE'S HOME SECURITY BUSINESS ACTIVITIES

BHE began publicly marketing its home security system, called CareTaker, in December 1995. This system includes anti-burglary, life/safety and home automation features. The basic package includes 24-hour monitoring, alarm panel, two door/window sensors, one smoke or freeze sensor, internal speaker and telephone control. If the sensors are triggered, a message is sent to a central processing unit that uses the phone lines to call a monitoring station in Rockford, Minnesota. The monitoring station then contacts the police, fire department, or homeowner as appropriate.

For this basic service, BHE charges an installation fee of $99 with a monitoring charge of $18.95 per month for five years (by contract). Other features are available at additional costs. BHE intends to join its CareTaker bills with BHE's electric bills.

IV. DEFINITION OF NON-CORE UTILITY ACTIVITIES

To establish procedures to govern the operation of non-core utility business ventures, such as CareTaker, we must define core

regulated service. We will define "core" electric utility service as:

> the generation, transmission and distribution of electricity to wholesale and retail customers, including customer service functions, such as billing and meter reading, that are associated with those activities.

The Public Advocate's witness Mr. Rubin proposed this definition and all other parties to this case agreed with it. As noted by Mr. Rubin, utility restructuring currently under consideration by the Maine Legislature may modify this definition. For the time being, however, we find it accurately describes the core activities of electric utilities. Any other services provided by a utility will be considered "non-core." Depending on the specific activity pursued by a utility, the Commission may decide, case by case, that there are exceptions to these definitions.

V. SEPARATE SUBSIDIARIES REQUIRED FOR NON-CORE UTILITY ACTIVITIES

As we stated in our July 12 Order on the scope of this proceeding, a primary focus of this proceeding is to establish requirements to insulate utility ratepayers from any financial

risks of the non-core venture. We find that the most effective way to do so is to require utilities to conduct non-core activities in a separate subsidiary.

A. Separate Subsidiary

The majority of the testimony from the parties in this case was about proper accounting methods to be used when a utility undertakes non-core utility activities *within* its corporate utility structure. Mr. Rubin and Mr. Cochrane each stated a preference for conducting non-core activities in a separate subsidiary. Mr. Rubin testified that, although possible, it was more difficult to ensure that accounting and customer-service protective measures are appropriate when all functions (core and non-core) are performed in one corporation. We find that requiring utilities to conduct non-core utility activities in a separate subsidiary will best protect utility customers from risks associated with non-core activities. Separate books and records will allow both the utility and the Commission to more easily track expenses and income associated with the non-core venture. Ratepayers may also achieve a degree of insulation from liabilities incurred by the non-core

subsidiary. Finally, a separate subsidiary may reduce any potential negative impact on the utility's cost of capital resulting from poor financial performance of the non-core activities.

There are certain transaction costs associated with establishing a separate subsidiary. Therefore, we do not require a separate subsidiary for each non-core activity. BHE may operate various non-core activities within one subsidiary or in multiple subsidiaries, as BHE prefers.

In establishing a subsidiary, BHE must comply with the requirements of 35-A M.R.S.A. §§ 707 and 708. The creation of a subsidiary is a reorganization subject to section 708. Transactions between the subsidiary and parent utility are subject to the requirements of section 707(3). We expect a subsidiary to fully reimburse the utility for any utility equipment, services and personnel used by the subsidiary. Any reimbursement methodology should, at a minimum, employ a fully distributed costing methodology.

The costing methodology required by the Federal Communications Commission (FCC) for telecommunication carriers to

separate their regulated costs from non-regulated costs provides a model.[2] This method directly assigns and apportions costs

[2]The FCC's rules require telecommunication carriers to follow the follow principles in allocating costs to regulated and non-regulated activities:

> (1) Tariffed services provided to a nonregulated activity will be charged to the nonregulated activity at the tariffed rates and credited to the regulated revenue account for that service.
>
> (2) Costs shall be directly assigned to either regulated or nonregulated activities whenever possible.
>
> (3) Costs which cannot be directly assigned to either regulated or nonregulated activities will be described as common costs. Common costs shall be grouped into homogeneous cost categories designed to facilitate the proper allocation of costs between a carrier's regulated and nonregulated activities. Each cost category shall be allocated between regulated and nonregulated activities in accordance with the following hierarchy:
>
> (i) Whenever possible, common cost categories are to be allocated based upon direct analysis of the origin of the cost themselves.
>
> (ii) When direct analysis is not possible, common cost categories shall be allocated based upon an indirect,

between the two operations (regulated and non-regulated). Costs are directly assigned when they can be identified as relating exclusively to one activity. Costs not identified solely with one activity are apportioned first on a cost-causative relationship and then, where cost drivers cannot be identified, on a general allocation based on the ratio of all directly assigned costs. This methodology protects ratepayers from subsidizing competitive ventures, allows ratepayers to participate in the economies of scale and scope that may result from the utility and its subsidiary, and encourages cost reductions that benefit ratepayers.

> cost-causative linkage to another cost category (or group of cost categories) for which a direct assignment or allocation is available.
>
> (iii) When neither direct nor indirect measures of cost allocation can be found, the cost category shall be allocated based upon a general allocator computed by using the ratio of all expenses directly assigned or attributed to regulated and nonregulated activities.

47 C.F.R. § 64.901(b)(1-3).

BHE has argued in this case that only the portion of indirect common costs that are incrementally higher due to non-core activity should be assigned to the non-core business. In theory, we do not disagree. If it were possible to accurately determine all incremental costs, including all opportunity costs, associated with a non-core venture, we would support such a methodology. It would, however, likely be difficult and controversial to capture *all* the appropriate costs. Using fully distributed costs builds a margin for error -- in favor of ratepayers -- into the allocation. If some variable costs are missed in the direct assignment, then ratepayers are still protected by allocating a portion of the costs found to be common. Moreover, it is at least possible that using fully distributed costs will reduce the heat of debates concerning what costs are direct and what costs are common, because even common costs are shared.

The Commission will review BHE's accounting methodology for CareTaker at the time it makes its required filings under 35-A M.R.S.A. § 707(3) relating to affiliated interest transactions.

B. Royalties

In addition to establishing requirements to ensure that the utility and its ratepayers are fully compensated for services provided by the utility to the non-core businesses, some commissions have required the non-core activity to pay a "royalty" to core customers (e.g., impute revenues in the form of a royalty payment).

Mr. Rubin recommends that royalties be examined case by case in an appropriate proceeding where the Commission can examine the cost allocation procedures of the utility, the extent to which the utility's name or other intangible assets are used by the non-core business and other relevant factors. CMP and BHE oppose the imposition of royalties.

We make no decision about imposing a royalty at this time, nor do we reach any conclusion about whether royalties are *ever* appropriate. The time for deciding this issue will be when reviewing a utility's cost allocation during a rate setting proceeding. If all costs have not been properly captured, we may consider imposing a royalty.

VI. BELOW-THE-LINE RATEMAKING TREATMENT

In this proceeding, all parties, except BHE, support "below-the-line" accounting treatment of all non-core utility business ventures. BHE recommends that the CareTaker program be accounted for "above-the-line."[3] The Commission has at least three choices with regard to ratemaking treatment of non-core activities: 1) account for non-core activities below-the-line; 2) account for non-core activities above-the-line, or 3) make no decision until the time of a rate case. From a ratepayer's perspective, rates are not affected by accounting for non-core activities above- or below-the-line, until the time of a rate case.

As described in our July 12, 1996 Order on the scope of this proceeding, our primary concern with regard to non-core activities is to "ensure that utility ratepayers are insulated from any financial risks of the non-core business venture." Below-the-line accounting (assuming perfect allocation of costs)

[3]"Below-the-line" treatment refers to keeping the costs and revenues of the non-core activity separate from those used in determining rates for core activities. "Above-the-line" treatment refers to including the costs and revenues of the non-core activity with those of the core activities for purposes of ratemaking.

allocates the potential risks and rewards of the non-core activities to shareholders alone and holds ratepayers indifferent to the presence of the non-core activity. Accordingly, we believe that non-core activities should generally be accounted for below-the-line. BHE should treat all expenses and revenues associated with CareTaker as below-the-line in its next rate proceeding.

VII. ACCOUNTING REQUIREMENTS

Chapter 310 of the Maine Public Utilities Commission's rules establishes a uniform system of accounts for electric utilities. Under this rule, each electric utility must keep its books in the manner and form prescribed by the Federal Energy Regulatory Commission (FERC). FERC requires electric utilities to separately account for non-utility operations. Similar requirements exist for gas utilities. *See* Chapter 410 of the Commission's Rules. We expect BHE to accurately account for its non-core ventures consistent with FERC's requirements.

VIII. REPORTING REQUIREMENTS

BHE's witnesses proposed that BHE notify the Commission 30 days prior to marketing any non-core business activities that

would require 1% or more of the Company's gross capitalization over five years. In its brief, BHE states that it would be willing to notify the Commission about smaller business ventures on or before the time it begins marketing. BHE is also willing to provide annual financial reports on all of its non-core businesses. CMP states that providing notice to the Commission on a basis contemporaneous with beginning a new business is appropriate and will allow the Commission to fulfill its general oversight responsibilities without regulating non-core activities. In its Exceptions to the Hearing Examiner's Report, CMP asked that notice be limited to 14 days prior to entering into a non-core business. Mr. Rubin suggests that utilities supplement their annual reports to provide specific information about non-core business ventures.

A. Notification

Utilities should notify the Commission of their intent to engage in any non-core business venture. This requirement will be satisfied when a utility files for sections 707 and 708 approvals of any subsidiary specific to one non-core business. If a utility chooses to engage in more than one non-core-business

activity under a single general purpose non-core-business subsidiary, it shall notify the Commission of each new non-core-business activity contemporaneous with the utility's first public expression of intent to engage in such activity.

Since BHE has already begun its CareTaker operation, prior notification is not possible. BHE, instead, should notify the Commission within 30 days of the date of this Order on its plans for bringing its CareTaker operations into compliance with the requirements in this Order.

B. Annual Report

As part of the annual report filed by utilities pursuant to Chapter 710 of the Commission's rules, BHE must include a brief description of each non-core activity.

IX. REQUIRED ADDITIONAL PROTECTIONS

A. Limits on Use of Customer Information

Mr. Rubin and Mr. Cochrane both recommended the Commission place limits on the use of core customer information for non-core ventures. According to Mr. Rubin, some types of information obtained by a utility in its core utility monopoly electric service business should be considered proprietary and

not be generally available for non-core business activities without customers' consent. Both Mr. Cochrane and Mr. Rubin listed some types of information that they considered to be private information, but neither offered a definition or a complete list. To determine the appropriate treatment of core customer-specific information (CSI) obtained by a utility, we

must define what information we consider private or in need of protection.

A similar issue was recently addressed in the Telecommunications Act of 1996 (the Act). The Act defines certain information as Customer Proprietary Network Information (CPNI).[4] CPNI is:

> [i]nformation that relates to the quantity, technical configuration, type, destination, and amount of use of a telecommunications service subscribed to by any customer of a telecommunications carrier, and that is made available to the carrier by the customer solely by virtue of the carrier-customer relationship.

47 U.S.C. § 222(f)(1)(A). Under the Act, carriers may not use individually identifiable CPNI except "as required by law or with the approval of the customer" for any purpose other than:

> (1) to initiate, render, bill and collect for telecommunications services;
>
> (2) to protect the carrier or user from fraud, abuse, or illegal use of such services; or

[4]The FCC has issued a Notice of Proposed Rulemaking (NPRM) in order to "specify in more detail and clarify the obligations" associated with protecting CPNI. An order regarding this is expected in the first quarter of 1997.

> (3) to provide any inbound telemarketing, referral, or administrative services on customer-initiated calls.

47 U.S.C. § 222(c),(d).

The Act does not prohibit telecommunications carrier from providing subscriber list information (names, telephone numbers, addresses of subscribers). 47 U.S.C. § 222(e). The Act also allows telecommunications carriers to use ***aggregate*** CPNI for purposes other than the above noted exceptions but only if, upon reasonable request, they provide the aggregate customer information to other carriers or persons on reasonable and nondiscriminatory terms and conditions. 47 U.S.C. § 222(c)(3).

Although the requirements described above relate to the telephone industry, we do not believe customers of other utilities should be treated differently. Further, electric utilities in Maine have repeatedly claimed that customer specific information should be treated as confidential. ***See, e.g.***, Hearing Examiner's Protective Order No. 1, Specific Customer Information, Docket No. 93-076. We agree that information obtained by the utility in its role as a utility, not otherwise publicly available, should be protected. Therefore, for the

purposes of this case, we will adopt the following definition for Customer Specific Information (CSI):

> CSI is information that relates to the usage, technical configuration, or type of electrical service subscribed to by any customer of an electric utility that is available to the utility solely by virtue of the utility-customer relationship.

In its Exceptions, CMP opposed the Hearing Examiner's proposed limits on the use of CSI because the Commission had excluded the impact on competitors from the scope of this proceeding. We do not find merit in this argument as we are not "protecting competitors" but rather are protecting ratepayers by ensuring that non-core ventures adequately reimburse the utility for use of utility information or has the ratepayer's permission to use the information.

Thus, to use any CSI, a non-core venture must purchase the CSI from the core company at market value, and to help determine market value the core company must make the CSI generally available under the same terms. To use customer-specific CSI (as distinguished from aggregated CSI) BHE must first obtain affirmative, written permission from the customer.

B. Licensure Requirements for BHE's CareTaker Installers

A number of parties to this proceeding raised concerns that BHE's non-core activities may be exempt from State electrician licensing requirements because those provisions generally do not apply to the electrical installations by public utilities. The Maine Electricians' Examining Board reached an agreement with BHE, CMP, and the Public Advocate that the practices at issue in this proceeding would not be exempt from licensure as the result of any action of this Commission. We agree that nothing in this Order affects applicable licensing requirements of the Maine Electricians' Licensing Board.

X. ADDITIONAL PROTECTIONS NOT REQUIRED AT THIS TIME

A. Separate Billing

Mr. Rubin recommended that utilities be prohibited from including non-core services on the same bill as core services in order to avoid customer confusion and to ensure that customers do not give away rights they have associated with their core utility service (e.g., payment arrangements, winter disconnection policy, etc.). Both BHE and CMP opposed this restriction claiming

customers desire such combined billing and that Chapter 81 already protects ratepayers that are billed for utility and non-utility services on a single bill. OPA, in its reply brief, withdrew its request to require such separate billing and instead reserved the right to request a rulemaking in the future. We agree that Chapter 81, §§ 2(L) and 3(K) adequately address the concern raised by Mr. Rubin and we will not require separate billing for non-core activities.

B. Approval if Non-Core Activities Exceed Set Percentage of a Utility's Capitalization

Mr. Rubin suggested that the Commission set a ceiling on the amount a utility may invest in non-core business ventures without obtaining prior Commission approval. Specifically, he recommended a limit of 5% of the utilities total capitalization. We find that such a limit is unnecessary given our requirements that non-core activities take place in a separate subsidiary. When we approve the creation of a subsidiary, we will also approve a limit on the amount the core utility can invest in the subsidiary. This will allow us to ensure that the non-core

utility does not unduly risk the financial integrity of the core business.

XI. CONCLUSION

This Order describes the requirements BHE must comply with in operating its security alarm business. It also sets forth the general principles we will likely apply to any utility conducting non-core utility ventures. These principles will be the subject of a generic rulemaking in the near future. In establishing these principles, we do not intend to discourage legitimate non-core business opportunities. Rather, our purpose is to ensure that ratepayers are insulated from the risks associated with such ventures. We believe the requirements we have established strike the proper balance by protecting BHE's core service customers while at the same time imposing only those conditions on BHE that are necessary so that we interfere with competitive markets as little as possible.

Accordingly, it is

O R D E R E D

1. That Bangor Hydro-Electric Company will operate its CareTaker non-core security alarm business in accordance with the requirements set forth in the body of this Order.

2. That BHE will notify the Commission within 30 days of the date of this Order on its plans for bringing in its CareTaker operation into compliance with this Order.

3. That this investigation opened on May 17, 1996, in response to a complaint filed by Mr. Cochrane and 23 other persons on February 2, 1996, is hereby closed.

Dated at Augusta, Maine, this 28th day of January, 1997.

BY ORDER OF THE COMMISSION

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Christopher P. Simpson
Administrative Director

COMMISSIONERS VOTING FOR: Welch
Nugent
Hunt

NOTICE OF RIGHTS TO REVIEW OR APPEAL

5 M.R.S.A. § 9061 requires the Public Utilities Commission to give each party to an adjudicatory proceeding written notice of the party's rights to review or appeal of its decision made at the conclusion of the adjudicatory proceeding. The methods of review or appeal of PUC decisions at the conclusion of an adjudicatory proceeding are as follows:

1. Reconsideration of the Commission's Order may be requested under Section 1004 of the Commission's Rules of Practice and Procedure (65-407 C.M.R.110) within 20 days of the date of the Order by filing a petition with the Commission stating the grounds upon which reconsideration is sought.

2. Appeal of a final decision of the Commission may be taken to the Law Court by filing, within 30 days of the date of the Order, a Notice of Appeal with the Administrative Director of the Commission, pursuant to 35-A M.R.S.A. § 1320 (1)-(4) and the Maine Rules of Civil Procedure, Rule 73 et seq.

3. Additional court review of constitutional issues or issues involving the justness or reasonableness of rates may be had by the filing of an appeal with the Law Court, pursuant to 35-A M.R.S.A. § 1320 (5).

Note: The attachment of this Notice to a document does not indicate the Commission's view that the particular document may be subject to review or appeal. Similarly, the failure of the Commission to attach a copy of this Notice to a document does not indicate the Commission's view that the document is not subject to review or appeal.